

## *Consumer and Community Affairs*

In 1998 the Board's activities in consumer and community affairs centered on reviewing applications for the acquisition of banking organizations, on improving disclosures to consumers about mortgage transactions, and on fair lending issues, including the material enhancement of the Board's enforcement capabilities.

As consolidation of the banking industry continued during 1998, the Board received applications for several exceptionally large mergers and acquisitions, and held public meetings on five of them. After extensive analysis, the Board approved all the applications, finding in each instance that approval was consistent with the convenience and needs of the communities to be served.

In July the Board and the Department of Housing and Urban Development (HUD) issued a report to the Congress suggesting legislative reforms to the Truth in Lending Act (which is administered by the Board) and the Real Estate Settlement Procedures Act (which is administered by HUD). The two agencies had earlier considered whether the disclosures required under these laws could be simplified and streamlined, either by regulatory or statutory amendment. After determining that regulatory change alone would not achieve the improvements called for by the Congress in 1996 legislation, the Board and HUD made recommendations on four key questions as a starting point for congressional consideration of statutory reform.

In the fair lending area, the Board's enforcement capabilities were materially enhanced with the adoption of new interagency examination procedures,

developed over the past two years by an interagency team. The Board referred one discrimination case involving a state member bank to the Department of Justice.

Acting on behalf of the Federal Financial Institutions Examination Council (FFIEC) and HUD, the Board prepared Home Mortgage Disclosure Act (HMDA) statements for individual lenders and aggregate reports for metropolitan areas. The statements reflected data reported in 1998 for the preceding year. These data indicated that denial rates continued to show disparities among racial and ethnic groups; the number of loans to black and Hispanic applicants increased in 1997 as in previous years, but the increases were modest compared with the average annual increase during the five years from 1993 through 1997.<sup>1</sup>

These matters are discussed below, along with other Board activities in the areas of consumer and community affairs.

### **Applications**

While most applications to the Board for approval of an acquisition are processed by a Reserve Bank under authority delegated by the Board, the Board itself considers applications for acquisitions that are exceptionally large or that raise substantive issues. As required by the Bank Holding Company Act (BHCA), the Board's consideration of

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1. The period 1993–97 is used for analysis of trends in HMDA data because HMDA coverage was expanded in 1993 to include a significantly larger group of independent mortgage companies.

such applications in 1998 takes account of specific factors, including the competitive effects of the acquisitions, the parties' financial and managerial resources, and the convenience and needs of the communities to be served, including the Community Reinvestment Act (CRA) performance records of the insured depository institutions involved. In addition to soliciting written comment from the public on these applications, in 1998 the Board held public meetings on five applications to give interested persons an opportunity to present oral testimony. After extensive analysis, the Board approved all the applications, finding in each case that approval was consistent with the factors prescribed by the BHCA, including the convenience and needs of the communities to be served.

- In April the Board approved the application by First Union Corporation, Charlotte, North Carolina, to acquire CoreStates Financial Corporation, Philadelphia, Pennsylvania.
- In August the Board approved the application by NationsBank Corporation, Charlotte, North Carolina, to acquire BankAmerica Corporation, San Francisco, California, a merger resulting in the nation's largest depository institution.
- In September the Board approved the application by Travelers Group, Inc., New York, New York, to acquire Citicorp, New York, New York. The resulting company, Citigroup, became the largest commercial banking organization in the world, offering not only banking but also securities and insurance services.
- Also in September the Board approved the application by Banc One Corporation, Columbus, Ohio, to acquire First Chicago NBD Corporation, Chicago, Illinois. This acquisition

created the largest banking organization in the Midwest and the fifth largest in the nation.

- In October the Board approved the application by Norwest Corporation, Minneapolis, Minnesota, to acquire Wells Fargo and Company, San Francisco, California.
- Also in October the Board approved the application by SunTrust Banks, Inc., Atlanta, Georgia, to acquire Crestar Financial Corporation, Richmond, Virginia.

These applications generated significant public interest. While they were supported by many commenters, adverse comment generally focused on anticipated job losses, branch closures, decreased lending, or other economic effects in the areas served by the organization being acquired. Commenters also criticized the CRA records of depository institutions involved in the acquisitions. Responding to such comment, some organizations pledged specific sums for future lending, investment, and services.

In each of these applications, the Board found the CRA records of the organizations involved to be consistent with approval. In the cases involving anticipated branch closures, the Board required that the merged organizations report, for a two-year period, all branch closures and consolidations resulting from the mergers.

In addition to these "megamergers," the Federal Reserve System acted on nineteen bank and bank holding company applications during 1998 that involved protests by members of the public concerning insured depository institutions' performance under the CRA and three applications that involved depository institutions' adverse CRA performance records. One other application involved both a CRA protest and an

adverse CRA performance record. The Federal Reserve reviewed another twenty-five applications involving fair lending and other issues related to compliance with consumer protection laws.<sup>2</sup>

### **TILA and RESPA Reform**

In July the Board and HUD submitted a report to the Congress concerning legislative changes to the Truth in Lending Act (TILA) and the Real Estate Settlement Procedures Act (RESPA) as these statutes apply to home-secured loans. The report responded to a congressional mandate for the Board and HUD to simplify and improve the disclosures required by the two laws and to create a single format for complying with them.

The agencies' report followed an eighteen-month study indicating that consumers primarily wanted disclosures about mortgage costs to be given earlier, so that they could comparison shop before applying for a loan from a particular lender. Consumers also wanted the cost disclosures to be as accurate as possible, so that they would not face unexpected charges at loan closing, when they no longer have the flexibility to seek other financing. Consumer advocates believed that the benchmark figure for comparison shopping—the annual percentage rate (APR)—should be retained and made more inclusive, and that any rate and other cost information provided at the time of application should be firm, subject to only limited conditions. They also believed that abusive lending practices should be addressed as part of any reform effort.

Many creditors asserted that the regulatory framework could be simplified by eliminating many of the disclosures, including the APR and finance charge items. They suggested that disclosures should focus instead on the interest rate, points, monthly payments, and settlement costs. To address concerns about the accuracy of settlement cost disclosures, some creditors favored a system of guaranteed costs in exchange for protection from RESPA's anti-kickback provisions. Other creditors and settlement service providers expressed concern that under such a plan they would be unable to compete with larger creditors and service providers.

The report to the Congress discussed ways to provide consumers with more meaningful and more timely cost information about home-secured transactions and at the same time ease compliance burdens on creditors. It contained recommendations addressing four key questions:

- Should the finance charge and APR disclosures be eliminated, or modified and retained? The Board and HUD recommended that the finance charge and APR concepts be retained and that the definition of the finance charge be expanded to include all costs the consumer is required to pay to obtain the loan, with limited exceptions. The agencies also recommended changes in the disclosures—such as including the contract interest rate, so that consumers can better understand the distinction between that rate and the APR.
- Should creditors be required to give firmer quotes for closing costs disclosed under RESPA? The Board and HUD recommended that creditors be required to give consumers more-reliable closing cost information, to promote shopping and competition.

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2. In addition, three applications were withdrawn in 1998—one involving an adverse CRA performance record and two involving issues with respect to compliance with consumer protection laws.

Currently, creditors provide a good faith estimate of closing costs, but there are no standards for accuracy. The agencies recommended that creditors be given a choice of either guaranteeing the settlement costs (with the possibility of relief from RESPA's anti-kickback provisions) or providing a good faith estimate that is accurate within a specified tolerance.

- Should the timing rules for providing cost disclosures to consumers be changed (and should creditors be required to provide disclosures before imposing substantial fees)? The Board and HUD recommended that consumers be given cost disclosures for any home-secured loan as early as possible in the shopping process. The Board recommended that the initial disclosures be provided not later than three days after application. In addition, the Board and HUD recommended that, three days before closing, creditors be required to redisclose significant changes in the APR or other material disclosures and to provide an accurate copy of the required HUD settlement statement. For home-secured transactions not involving a home purchase, the Board recommended that, three days before closing, consumers also receive a notice of a pre-closing right to a refund of fees paid that in most instances would substitute for the existing right to rescind the transaction and receive a refund.
- Should additional substantive consumer protections be added to the statutes to address abusive lending practices? The Board and HUD recommended the adoption of substantive protections that target abusive lending practices without unduly interfering with the flow of credit, creating unnecessary creditor burden, or narrowing consumers' options in

legitimate transactions. The agencies specifically recommended extending restrictions on balloon payments for loans subject to the Home Ownership and Equity Protection Act (HOEPA); prohibiting the advance collection of lump-sum credit-insurance premiums for HOEPA loans; and requiring certain minimum standards for the notice of home foreclosures that creditors must provide.<sup>3</sup>

The Board and HUD presented their recommendations in hearings before subcommittees of the House Committee on Banking and Financial Services and the Senate Committee on Banking, Housing, and Urban Affairs. The agencies suggested that the Congress use the recommendations as a starting point for considering legislative changes.

## **Regulatory Matters**

The Board has responsibility for implementing federal laws concerning consumer financial services and fair lending. In 1998, significant regulatory developments in these areas included the following:

- Mandatory compliance with comprehensive new rules under Regulation M (Consumer Leasing) became effective January 1, 1998.
- In March the Board published an advance notice of proposed rulemaking, announcing a comprehensive review of Regulation B (Equal Credit Opportunity). The notice solicited comment on several specific issues, including lenders' pre-application marketing practices and whether the

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3. Enacted in 1994, HOEPA amended the TILA to require additional disclosures and provide for substantive restrictions on nonpurchase-money home loans that involve rates or fees above a certain amount.

current prohibition on creditors' collecting race and similar information about applicants for nonmortgage credit products should be removed.

- In March the Board published an advance notice of proposed rule-making, launching a comprehensive review of Regulation C (Home Mortgage Disclosure). The review will identify ways in which the Board could revise the regulation to clarify and simplify the regulatory language, respond to technological and other developments, reduce undue regulatory burden on the industry, eliminate obsolete provisions, and improve the quality and usefulness of the data collected under the regulation. The Board solicited comment on several specific issues, such as whether to require creditors to collect and report data on pre-approvals and whether to modify the current reporting categories applicable to refinancings and home improvement loans.
- In March the Board issued a proposal to permit the electronic delivery of disclosures for Regulations B, M, Z (Truth in Lending), and DD (Truth in Savings). The proposal would allow financial institutions, creditors, and others—with the consumer's consent—to provide electronically the information required by these regulations. This information could include such items as initial disclosures of terms and conditions of accounts, loans, and leases; periodic statements of account activity; and notices about error resolution. The proposal corresponds in approach to an interim rule, also published in March, amending Regulation E (Electronic Fund Transfers). The Board received more than 200 public comments on the proposal and the interim rule. Commenters generally supported modifying the regulations to permit the electronic delivery of disclosures but expressed concerns about how the rules would apply in particular circumstances.
- In September the Board published revisions to Regulation E reducing the time periods for investigations of claimed errors involving consumers' use of debit cards at point-of-sale and in foreign-initiated transactions. The revised rule requires a financial institution to provisionally credit an account within ten business days—rather than twenty, as the regulation permitted formerly—if the institution has not resolved the error claim within that time. To address commenters' concerns about the amount of time necessary to complete an investigation, the revised rule leaves in place a provision that gives institutions up to ninety calendar days to complete the investigation. At the same time, the Board adopted a rule that increases the time period for investigating errors claimed within thirty days after a consumer has opened an account; this rule was issued to address fraudulent claims of error on new accounts. Under the rule, an institution has up to twenty business days—rather than the ten formerly permitted—to resolve an alleged error before it must provisionally credit funds. It also has up to ninety calendar days to complete the investigation, rather than forty-five days.

In addition, the Board took the following regulatory actions:

- Adopted amendments to the model forms in Regulation B related to consumer rights under the Fair Credit Reporting Act
- Published technical amendments to Regulation M that clarify the rules for disclosing scheduled lease payments

and the disclosure requirements for advertisements

- Updated the official staff commentary to Regulation Z to give guidance on disclosures for open-end credit plans that offer deferred payment features or that permit creditors to increase rates when consumers make late payments or exceed established credit limits, and to address the treatment of annuity costs in reverse mortgage transactions and transaction fees imposed on checking accounts with overdraft protection
- Adopted amendments to Regulation DD to implement minor changes to the Truth in Savings Act contained in the Economic Growth and Regulatory Paperwork Reduction Act of 1996
- Made final an interim rule (adopted in 1995) on the disclosure of the annual percentage yield for certain certificates of deposit that have maturities greater than one year and that do not compound interest.

Also, in March the Board reported to the Congress on the ways in which it assists small entities regarding compliance with Board regulations. The report was required under the Small Business Regulatory Enforcement Fairness Act of 1996. The Board reported that, in accordance with the Federal Deposit Insurance Act, it ordinarily will reduce civil penalties against small entities from the amount that would be assessed against larger entities, or may waive them altogether. But the Board will not reduce or waive these penalties when aggravating factors exist. Guidance to small entities is available from the Federal Reserve through conferences or training for bankers; review of submitted forms and other documents; educational advisory visits to banks; brochures, compliance guides, and newsletters; and telephone responses to calls and letters.

## **HMDA Data and Lending Patterns**

The Home Mortgage Disclosure Act requires mortgage lenders covered by the act to collect and make public certain data about their home purchase, home improvement, and refinancing loan transactions. Depository institutions generally are covered if they were located in metropolitan areas and met the asset threshold at the end of the preceding year. For 1997, the asset threshold for depository institutions was \$28 million. Mortgage companies are covered if they were located in or made loans in metropolitan areas and had assets of more than \$10 million (when combined with the assets of any parent company) at the end of the preceding year; and they are covered, regardless of asset size, if they originated 100 or more home purchase loans in the preceding year.

In 1998, 6,886 depository institutions and affiliated mortgage companies and 1,039 independent mortgage companies reported HMDA data for calendar year 1997 to their supervisory agencies. These lenders submitted information about the geographic location of the properties related to their loans and applications, the disposition of loan applications, and, in most cases, the race or national origin, income, and sex of applicants and borrowers. The Federal Financial Institutions Examination Council processed the data and produced disclosure statements on behalf of HUD and the FFIEC's member agencies.<sup>4</sup>

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4. The member agencies of the FFIEC are the Board, the Federal Deposit Insurance Corporation (FDIC), the National Credit Union Administration (NCUA), the Office of the Comptroller of the Currency (OCC), and the Office of Thrift Supervision (OTS).



The FFIEC prepared individual disclosure statements for each lender that reported data—one statement for each metropolitan area in which the lender had offices and reported loan activity. In July, each institution made its disclosure statement public; in August, reports containing aggregate data for all lenders in a given metropolitan area were made available at central depositories in the nation's approximately 330 metropolitan areas. These data were used not only by the FFIEC member agencies, the reporting institutions, and the public, but also by HUD in its oversight of Fannie Mae and Freddie Mac and by HUD and the Department of Justice as one component of fair lending reviews. The data also assisted HUD, the Department of Justice, and state and local agencies in responding to allegations of lending discrimination and in targeting lenders for further inquiry.<sup>5</sup>

The data reported in 1998 for the prior year included 16.4 million reported loans and applications, an increase of about 11 percent over 1996, due primarily to increased refinancing activity. The number of home purchase loans extended in 1997 compared with 1996 increased 12 percent for Asians, 4 percent for blacks and Hispanics, and 2 percent for whites, while decreasing 1 percent for Native Americans. Over the five years from 1993 through 1997, the number of home purchase loans extended increased 62 percent for blacks, 58 percent for Hispanics, 29 percent for Asians, 25 percent for Native Americans, and 16 percent for whites.

The number of home purchase loans extended to applicants in all income categories increased in 1997 compared with the preceding year. The number of such loans extended to lower-income applicants increased 6 percent, and the number extended to upper-income applicants increased 5 percent. Over the five years from 1993 to 1997, the number of home purchase loans extended to lower-income and upper-income applicants increased 38 percent and 27 percent respectively.

In 1997, 34 percent of Hispanic applicants and 26 percent of black applicants for home purchase loans sought government-backed mortgages; the comparable figures for white applicants, Asian applicants, and Native American applicants were 15 percent, 12 percent, and 11 percent, respectively. Twenty-seven percent of lower-income applicants for home purchase loans applied for government-backed loans in 1997, compared with 11 percent of upper-income applicants.

Denial rates for conventional (non-government-backed) home purchase loans in 1997 were 53 percent for black applicants, 52 percent for Native American applicants, 38 percent for Hispanic applicants, 26 percent for white applicants, and 13 percent for Asian applicants. Except for Asian applicants, each of these rates exceeded the comparable rate for 1996.

Overall, the denial rate for conventional loans was 29 percent in 1997. This rate has increased in each of the past several years, reflecting, in part, the increasing share of applications for conventional loans filed by lower-income applicants.

In recent years, a growing share of the applications reported under HMDA has been filed with lenders that specialize in manufactured housing and subprime lending. In 1997, these lenders

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5. On behalf of the nation's eight active private mortgage insurance (PMI) companies, the FFIEC also compiles information on applications for PMI similar to the information on home mortgage lending collected under HMDA. Lenders typically require PMI for conventional mortgages that involve small downpayments.

denied 56 percent of all applications for conventional home purchase loans they received, compared with 12 percent for other lenders.

## **Fair Lending**

The Board's fair lending activity during 1998 focused on enhanced enforcement capabilities, referrals to the Department of Justice, and consumer education.

### **Examination Procedures**

During 1998 the Board adopted new procedures for fair lending examinations. The new procedures' principal analytical technique calls for examining the files of denied applications, identifying the minority applicant with the least deficient credit record for a given denial reason, and comparing that applicant's record against nonminority applicants whose credit records were more deficient, relative to the same denial reason, and yet were approved for credit. Variations of this technique will be employed in examining for potential discrimination in pricing, commercial lending, and credit-scored products and for redlining analysis. The new procedures were field-tested during 1998 in several Federal Reserve Districts and will be in effect for all compliance examinations begun after January 1, 1999. To prepare examiners for the new procedures, the Board over the past year developed and implemented two training programs for fair lending.

The Board also made important enhancements to the statistical regression program used to aid examiners in assessing fair lending compliance among large-volume mortgage lenders. For example, a methodology for analyzing discrimination in loan pricing was added to the program's existing methodology for the analysis of apparent dis-

criminatory disparities in application denials. In addition, efforts continued in 1998 to achieve closer matching of minority and nonminority applicants for comparative analysis through adjustments to the type and number of factors (or variables) used in the regression. Finally, significant work was done on developing a regression methodology for use in examining groups of loan transactions that included too few denied applications to permit use of the existing regression format. This latter effort addressed a recurring limitation on the use of regression analysis.

### **Referrals to the Department of Justice**

Under the 1991 amendments to the Equal Credit Opportunity Act, the Board refers to the Department of Justice violations that it believes may constitute a "pattern or practice" of discrimination. Potential referral cases identified during Federal Reserve compliance examinations are sent to the Board for review and a determination as to whether there is "reason to believe" that a pattern or practice warranting referral has occurred. Of the sixteen cases reviewed by the Board in 1998, three involved complicated fact patterns regarding the acceptance or denial of loan applications and eight raised issues of potentially discriminatory pricing identified through review of bank policies and analysis of loan files. One case was referred to the Department of Justice in 1998; it involved the failure of a credit card issuer to consider child support payments as income. Four cases were still under investigation at year-end.

### **Consumer Education**

In 1998 an interagency Fair Lending Task Force prepared a booklet on mort-



gage loan pricing, *Looking for the Best Mortgage—Shop, Compare, Negotiate*. The booklet tells prospective loan applicants how mortgage loans are priced, how to obtain and compare price information from different lenders, and how to negotiate the best price. It focuses on such pricing practices as “overages,” which have been the subject of recent regulatory agency fair lending investigations. It also advises consumers about the applicability of the fair lending laws to the loan-pricing practices of mortgage lenders.

### Community Development

Through its community affairs program, the Federal Reserve conducts ongoing outreach, informational, and educational activities to help financial institutions and the public understand and address financial services issues affecting low- and moderate-income persons and communities. In 1998 the Board and the Reserve Banks began a Systemwide strategic planning process to re-examine their mission in regard to community affairs and to develop strategies for responding better to emerging financial services issues.

Throughout 1998, educational and technical assistance activities focused increasingly on small business and economic development in low- and moderate-income and rural communities. For example,

- The Federal Reserve Bank of Cleveland began the implementation phase of its “Access to Capital Initiative,” a joint effort with the Small Business Administration and the Greater Cleveland Growth Association’s Council of Smaller Enterprises. The initiative was designed to help expand small business access to technical assistance on financing and business development. Recommendations and action

plans were developed at a meeting of more than 175 bankers, small business finance intermediaries, venture capitalists, accountants, attorneys, public officials, and business owners.

- The Chicago Reserve Bank began planning its “Small Business Credit Access Initiative.” This initiative seeks to identify and address barriers to equity and debt capital for small enterprises in the Chicago metropolitan area, especially businesses located in predominantly minority and low- and moderate-income communities.
- The Richmond Reserve Bank, in conjunction with the National Association of Women Business Owners, conducted a series of six conferences on “Access to Capital: Start to Finish,” which focused on the financing needs of and resources for women-owned businesses.
- The Boston Reserve Bank sponsored a conference, “Making It in the Mainstream,” that reviewed partnerships between minority business enterprises and major corporations as a strategy for inner-city business development and job creation.

Several educational programs focused on financial and technical assistance to help very small and start-up businesses. For example,

- The Minneapolis Reserve Bank sponsored a conference on small business development.
- The Atlanta Reserve Bank conducted a workshop on issues affecting micro-enterprise lending, and the Boston Reserve Bank developed a training curriculum on lending and the provision of technical assistance for organizations that offer services to microentrepreneurs.

Rural community development was the focus of several educational programs and publications. For example,

- The Kansas City Reserve Bank's community affairs and economic research departments worked together to sponsor a conference, "Equity for Rural America: From Main Street to Wall Street," to explore how rural communities can gain access to equity capital markets to strengthen local economies.
- The St. Louis Reserve Bank produced the *Community Development Resource Guide: A Rainbow of Opportunity in the Delta*, a resource focusing on organizations and financial resources available in the lower Mississippi Delta region. The Bank also conducted community development workshops that highlighted many of the successful initiatives that are helping to revitalize that region.

Several Reserve Banks' educational programs explored techniques for helping low-income persons move into mainstream employment and the financial services markets. For example, the Richmond Reserve Bank, together with Virginia Commonwealth University, sponsored a symposium on the "Delivery of Financial Services in a Post-Welfare Reform Society." Participants discussed means of serving individuals who do not have transaction accounts with depository institutions; the effects that trends toward electronic benefits transfer and other electronic banking trends will have on low- and moderate-income households; and techniques for helping low-income persons build financial assets.

Three Reserve Banks continued their long-term efforts to facilitate community and economic development on Indian reservations:

- The San Francisco Reserve Bank joined with the Affiliated Tribes of Northwest Indians to conduct four workshops on "Sovereign Lending"

for bankers and tribal leaders, to help facilitate lending by financial institutions in Indian Country.

- The Minneapolis Reserve Bank cosponsored, with the Federal Deposit Insurance Corporation (FDIC), two roundtables for Montana bankers on lending in Indian Country, with an emphasis on small business financing and economic development; and continued to work on community development issues at the Pine Ridge Reservation. The Reserve Bank also continued to develop a personal finance course to be offered at the Fond du Lac Tribal Community College.
- The Kansas City Reserve Bank drafted a case study focusing on community development issues encountered by Native Americans for use in educational programs in Indian Country.

Other educational programs focused on community development and reinvestment tools and techniques. For example,

- The Philadelphia Reserve Bank convened a workshop for Philadelphia-area nonprofit community development organizations and local bankers to share information on potential projects and financing opportunities.
- The Dallas Reserve Bank sponsored a workshop on "Asset-Based Community Development: Mobilizing an Entire Community," which focused on ways to strengthen community-led development of affordable housing and small business initiatives in the Dallas-Ft. Worth area.
- The San Francisco Reserve Bank, in cooperation with the University of California at Berkeley and the Institute of Urban and Regional Development, conducted the National Community Development Lending

School—a weeklong training program for lenders engaged in financing affordable housing, small businesses, commercial development, and community facilities in the community development context.

Overall during 1998, Reserve Banks sponsored or cosponsored 280 conferences, seminars, and informational meetings on community and economic development, reinvestment, and fair lending topics. More than 12,900 bankers, examiners, and participants from small businesses and community and consumer groups attended. Board and Reserve Bank community affairs staff also made presentations at conferences, seminars, and meetings sponsored by banking, governmental, business, and community organizations.

The Board and Reserve Banks provided in-depth technical assistance to bankers and community organizations on a variety of housing, community, and economic development issues. For example, the Atlanta Reserve Bank assisted bankers in their efforts to create bank and bank holding company community development corporations, and provided guidance on the financial structure of housing projects qualifying for federal low-income housing tax credits.

Also during 1998, Board and Reserve Bank community affairs staff conducted more than 1,600 outreach meetings with financial institutions, community development organizations, small businesses, public-sector agencies, academic institutions and foundations, and consumer and community groups to discuss community credit needs and issues related to the provision of financial services. In conjunction with these outreach efforts, several Reserve Banks developed or updated community profiles that identify key community and economic

development needs and describe resource organizations in selected communities. These profiles are made available to banks and to community and business organizations, and often help stimulate collaborative approaches to community reinvestment.

The Reserve Banks issued a variety of publications and other resources to provide bankers and community development organizations with information about community development issues and opportunities. For example,

- The Richmond Reserve Bank published two *MarketWise Reports*. One focused on development opportunities associated with the redevelopment of environmentally damaged areas (called “brownfields”); the other summarized survey data on the credit needs of small businesses and provided information on financial resources and technical assistance available to small firms.
- The Chicago Reserve Bank produced a videotape, *To Their Credit: Women-Owned Businesses*, designed to heighten awareness among lenders about barriers affecting the loan application process for women-owned businesses and to encourage and facilitate small business lending affiliations.
- The New York Reserve Bank published a *Directory of Small Business Assistance Resources for Northern New Jersey*.

The Reserve Banks published a total of twelve community affairs newsletters dealing with various aspects of community and economic development, reinvestment, and fair lending topics. The average combined circulation of these newsletters in 1998 was more than 67,000 bankers, small-business owners, housing, community and economic development officials, and community-

based development and consumer groups.

Community affairs staff members in 1998 continued to support the Federal Reserve's supervisory responsibilities. For example,

- They joined in reviewing proposals for community development initiatives from banks and bank holding companies, and assisted examiners by providing community contact and other information useful in CRA examinations.
- At several Reserve Banks, they assisted in conducting analyses of HMDA and CRA small business lending data.
- They held meetings with national organizations representing property insurers and appraisers to discuss issues and recommendations emerging from Mortgage Credit Partnership Projects, two-year efforts coordinated by six Reserve Banks to help identify and address barriers to equal access to credit in the homebuying process in selected cities.
- At the New York, Philadelphia, Chicago, Minneapolis, and San Francisco Reserve Banks, they arranged public meetings associated with Board consideration of applications for mergers involving major bank holding companies.

Board and Reserve Bank staff continued to provide support to members of the Board and Reserve Bank presidents on community development and financial services issues affecting low- and moderate-income households and communities. Their efforts included support for the Conference of Presidents' Subcommittee on Community Affairs; assistance with speeches and presentations by Board members before conferences and meetings of community, consumer, and civil rights groups; help in connec-

tion with tours by Board members of low- and moderate-income neighborhoods and community development projects; and support for a Board member who serves as Chairman of the Board of Directors of the Neighborhood Reinvestment Corporation.

### **Economic Effects of the Electronic Fund Transfer Act**

As required by statute, the Board monitors the effects of the Electronic Fund Transfer Act (EFTA) on the compliance costs and consumer benefits related to electronic fund transfer (EFT) services. In 1998 the economic effects of the EFTA likely continued to increase because of the continued growth of EFT services.

The Board approved two amendments to Regulation E involving the resolution of billing errors claimed by consumers. (See "Regulatory Matters.") Neither amendment is expected to have a negative economic effect. There were no changes to the EFTA in 1998.

Results of consumer surveys (most recently in 1996) indicate that during this decade the proportion of U.S. households using EFT services has grown at an annual rate of about 2 percent. About 85 percent of households have one or more EFT features on their accounts at financial institutions. Automated teller machines (ATMs) remain the most widely used EFT service. Over the past year, the number of ATM transactions increased about 2 percent, from 910 million a month in 1997 to 930 million a month in 1998. Over the same period the number of installed ATMs rose 13 percent, to 187,000. Direct deposit is another widely used EFT service: More than half of all households in the United States have funds deposited directly into their accounts. Use of the service is particularly widespread in the public sector,

accounting for more than half of social security payments and two-thirds of federal salary and retirement payments. Taking into account both public and private payments, the proportion of households receiving direct deposits has grown about 5 percent a year in this decade. About one-third of U.S. households have debit cards, which consumers use at merchant terminals to debit their transaction accounts. Such point-of-sale (POS) systems still account for a fairly small share of electronic transactions, but their use continued to grow rapidly in 1998. Over the past year, the number of POS transactions rose 25 percent, from about 120 million a month in 1997 to 150 million a month, and the number of POS terminals rose 31 percent, to 1.7 million.

The incremental costs associated with the EFTA are difficult to quantify because no one knows how industry practices would have evolved in the absence of statutory requirements. The benefits of the EFTA are also difficult to measure because they cannot be isolated from consumer protections that would have been provided in the absence of regulation. The available evidence suggests no serious consumer problems with EFT at present. (See "Agency Reports on Compliance with Consumer Regulations.")

## **Compliance**

During 1998, the Board's compliance activities included examinations, examiner training, and participation in the compliance activities of the Federal Financial Institutions Examination Council, including activities promoting increased uniformity in Community Reinvestment Act examinations.

## **Compliance Examinations**

Since 1977 the Federal Reserve has maintained a compliance examination

program to ensure that state member banks and foreign banking organizations subject to Federal Reserve examination comply with federal laws protecting consumers in the provision of financial services. During the 1998 reporting period (July 1, 1997, through June 30, 1998), the Federal Reserve conducted 546 examinations for compliance with consumer protection laws: 416 of state member banks and 130 of foreign banking organizations.<sup>6</sup>

## **Examiner Training**

Examiner training in consumer protection laws, fair lending laws, and the CRA is an important aspect of the Federal Reserve's compliance program. New Reserve Bank examiners attend a two-week basic compliance course; and examiners with six to twelve months of field experience attend a two-week advanced course, a two-week course in examination techniques for fair lending, and a one-week course in CRA examination techniques. During the 1998 reporting period, the Federal Reserve conducted two basic compliance courses with a total of thirty-four participants, two advanced compliance courses with a total of forty-one participants, two courses in fair lending examination techniques with a total of twenty-eight participants, and three courses in CRA examination techniques with a total of sixty-one participants.

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6. The foreign banking organizations examined by the Federal Reserve are organizations operating under section 25 or 25(a) of the Federal Reserve Act (Edge Act or agreement corporations) and state-chartered commercial lending companies owned or controlled by foreign banks. These institutions are not subject to the CRA and, typically, in comparison with state member banks, engage in relatively few activities that are covered by consumer protection laws.

## Participation in FFIEC Activities

The FFIEC is charged with developing uniform examination principles, standards, and report forms. In 1998, the member agencies of the FFIEC jointly revised examination procedures to reflect changes in consumer protection laws and regulations, including the Real Estate Settlement Procedures Act and the Electronic Fund Transfer Act. In addition, the FFIEC revised its policy guide, *Administrative Enforcement of the Truth in Lending Act—Restitution*, for the first time since 1980.

During 1998 the Board also participated in the FFIEC's efforts to promote consistency among the agencies in reporting CRA ratings information to the public—in particular, in developing a page on the Internet for CRA ratings (<http://www.ffiec.gov/cracf/crarating/main.cfm>).

The FFIEC worked during 1998 to foster consistency in the application of large-bank CRA examination procedures, which became fully effective on July 1, 1997. As part of this effort, the Board, the FDIC, the OCC, and the OTS reviewed performance evaluations for institutions examined under the lending, investment, and service tests; they also conducted eight joint examinations. The agencies found that examiners are generally conducting examinations in accordance with interagency CRA examination procedures for large retail institutions and the interagency questions and answers; some minor differences were noted among the performance evaluations reviewed and among the examiners participating in the joint examinations. In October, the agencies held an interagency examiner forum to discuss the results of the performance evaluation review and the joint examinations, as well as to develop recommendations for refining examiner guidance

for large institutions. Interpretive guidance on issues identified through these efforts will be issued in 1999.

## Community Reinvestment Act

The Federal Reserve assesses the Community Reinvestment Act performance of state member banks during regular compliance examinations and takes their CRA ratings (as well as other factors) into account when acting on applications from state member banks and from bank holding companies for mergers, acquisitions, and certain other actions.

The Federal Reserve has a three-faceted program for fostering better bank performance under the CRA:

- Examining institutions to assess compliance with the CRA
- Disseminating information on community development techniques to bankers and the public through community affairs offices at the Reserve Banks
- Performing CRA analyses in connection with applications from banks and bank holding companies.

During the 1998 reporting period (July 1, 1997, through June 30, 1998), the Federal Reserve conducted 410 CRA examinations. Of the banks examined, 96 were rated "outstanding" in meeting community credit needs, 308 were rated "satisfactory," 5 were rated "needs to improve," and 1 was rated as being in "substantial noncompliance."

## Agency Reports on Compliance with Consumer Regulations

The Board is required to report annually on compliance with Regulation B, which implements the Equal Credit Opportunity Act (ECOA); Regulation E, which implements the Electronic Fund Transfer Act (EFTA); Regulation M,



which implements the Consumer Leasing Act (CLA); Regulation Z, which implements the Truth in Lending Act (TILA); Regulation CC, which implements the Expedited Funds Availability Act (EFAA); Regulation DD, which implements the Truth in Savings Act (TISA); and Regulation AA, which targets unfair and deceptive practices. The Board assembles data on compliance from the Reserve Banks and also collects compliance data from the FFIEC agencies and other federal supervisory agencies.<sup>7</sup>

Summarized below are the reported compliance data for the period July 1, 1997, through June 30, 1998 (referred to below as the 1998 reporting period, or sometimes simply as 1998). The overall level of compliance in 1998 was similar to the overall level in 1997, but, as in past years, the level of compliance varied considerably from regulation to regulation.

### Regulation B (Equal Credit Opportunity)

The FFIEC agencies reported that 79 percent of the institutions examined during the 1998 reporting period were in compliance with Regulation B, compared with 80 percent for the 1997 reporting period. Of the institutions not in compliance, 69 percent had one to five violations. The most frequent violations involved the failure to take one or more of the following actions:

- Provide a written notice of credit denial or other adverse action containing a statement of the action taken, the name and address of the creditor,

a Regulation B notice, and the name and address of the federal agency that enforces compliance

- Collect information for monitoring purposes about the race or national origin, sex, marital status, and age of applicants seeking credit primarily for the purchase or refinancing of a principal residence
- Notify the credit applicant of the action taken within the time frames specified in Regulation B
- Give a statement of reasons for credit denial or other adverse action that is specific and indicates the principal reasons for the credit denial or other adverse action
- Take a written credit application for the purchase or refinancing of a principal residence
- Refrain from requesting the race, color, religion, national origin, or sex of an applicant in transactions not covered by the monitoring requirements.

The Office of Thrift Supervision (OTS) issued two formal enforcement actions that contained provisions relating to Regulation B.

The Federal Trade Commission (FTC) filed a complaint in a federal district court charging a mortgage lender in the Washington, D.C., area with violations of the ECOA, including, among others, failing to take written applications for mortgage loans, failing to collect monitoring information on mortgage loan applicants, and providing inadequate notices of adverse action to loan applicants. The FTC is seeking civil money penalties and injunctive relief.

The FTC also participated in credit-related seminars organized by the Congressional Black Caucus and released a new publication, *Bound for Good Credit*, designed to educate consumers

7. The agencies use different methods to compile compliance data. Accordingly, the data—which are presented here in terms of percentages of financial institutions supervised or examined—support only general conclusions.

on credit-related issues. In addition, the FTC is continuing its work with other government agencies and with creditor and consumer organizations to increase awareness of and compliance with the ECOA.

The other agencies that enforce the ECOA—the Farm Credit Administration (FCA), the Department of Transportation (DOT), the Securities and Exchange Commission (SEC), the Small Business Administration, and the Grain Inspection, Packers and Stockyards Administration of the Department of Agriculture—reported substantial compliance among the entities they supervise. The FCA's examination and enforcement activities revealed certain violations of the ECOA, most of them due to creditors' failure to collect information for monitoring purposes and to comply with rules regarding adverse action notices; however, no formal actions were initiated. The SEC reported that no violations of the ECOA were detected in examinations of registered broker-dealers conducted by self-regulatory organizations, the SEC's principal method of reviewing for compliance.

### Regulation E (Electronic Fund Transfers)

The FFIEC agencies reported that approximately 96 percent of the institutions examined during the 1998 reporting period were in compliance with Regulation E, compared with 94 percent for the 1997 reporting period. Financial institutions most frequently failed to comply with the following requirements:

- Investigate an alleged error promptly after receiving a notice of error, determine whether an error was actually

made, and transmit the results of the investigation and determination to the consumer within ten business days

- Provide customers with a periodic statement of all required information at least quarterly, or monthly if EFT activity occurred.

The OTS issued two formal enforcement actions that contained provisions relating to Regulation E during the 1998 reporting period. The FTC issued final decisions and orders with three Internet service providers settling charges that these companies violated the EFTA; specifically, the companies' "free trial" offers for on-line service resulted in unexpected charges for many consumers because the providers failed to make clear that consumers had an affirmative obligation to cancel before the trial period ended. The SEC reported that no violations of Regulation E were detected in examinations of registered broker-dealers conducted by self-regulatory organizations.

### Regulation M (Consumer Leasing)

The FFIEC agencies reported substantial compliance with Regulation M for the 1998 reporting period. As in 1997, more than 99 percent of the institutions examined were in compliance. The few violations involved failures to adhere to specific disclosure requirements.

In 1998 the FTC issued final decisions and orders in thirteen administrative cases concerning alleged deceptive lease or credit advertising, specifically, failure to clearly and conspicuously disclose and make available advertised lease and credit terms, in violation of the CLA or the TILA. Final decisions and orders issued by the FTC in 1998 settled charges against two

major automobile manufacturers, and five dealerships and their chief executive officers in the St. Louis area, for violations of the CLA and the TILA involving misrepresentation and hiding or failing to disclose adequately the terms of advertised automobile lease deals.

The FCA reported that it identified no violations of the CLA during its examinations in 1998.

### Regulation Z (Truth in Lending)

The FFIEC agencies reported that 74 percent of the institutions examined during the 1998 reporting period were in compliance with Regulation Z, compared with 75 percent in 1997. The Board and the OTS reported increases in compliance, the OCC and the FDIC reported decreases, and the NCUA reported an unchanged level of compliance. The FFIEC agencies indicated that of the institutions not in compliance, 62 percent had one to five violations, the same as in 1997.

The violations of Regulation Z most often observed were failures to comply with the following requirements:

- Accurately disclose the finance charge, payment schedule, annual percentage rate, security interest in collateral, and amount financed
- Accurately itemize the amount financed upon request
- Provide disclosures within three business days of application for RESPA-related residential mortgage applications
- Redisclose the annual percentage rate when a change occurred before consummation or settlement
- Withhold loan funds until the end of the rescission period.

The OTS issued two formal enforcement actions that contained provisions relating to Regulation Z. A total of 205 institutions supervised by the Board, the FDIC, or the OTS were required, under the Interagency Enforcement Policy on Regulation Z, to refund \$2.3 million to consumers in 1998 because of improper disclosures.

The FTC filed a complaint in federal district court charging a mortgage lender in the Washington, D.C., area, and its owner, with violating the TILA in connection with alleged deceptive and unfair practices in home mortgage lending. The FTC also issued final decisions and orders in thirteen administrative cases concerning alleged deceptive lease or credit advertising that involved the failure to clearly and conspicuously disclose and make available advertised lease and credit terms, in violation of the CLA or the TILA.

During 1998 the FTC also issued three publications informing consumers about home equity loans and reverse mortgages. In addition, the FTC issued a news release to customers of two airlines to assist them in exercising their rights under the Fair Credit Billing Act provisions of the TILA.

The Department of Transportation (DOT) continued during 1998 to prosecute an ongoing formal enforcement proceeding instituted in 1993 against a travel agency and a charter operator. The complaint in this proceeding alleged that the two organizations had violated Regulation Z by routinely failing to send credit statements for refund requests to credit card issuers within seven days of receiving fully documented credit refund requests from customers. A motion filed by the DOT before an administrative law judge for summary judgment was denied. The DOT is currently in negotiations to settle this litigation.

### Regulation CC (Expedited Funds Availability)

The FFIEC agencies reported that 89 percent of institutions examined during the 1998 reporting period were in compliance with Regulation CC, compared with 87 percent in the 1997 reporting period. Of the institutions not in compliance, 65 percent had one to five violations. Institutions most frequently failed to comply with the following requirements:

- Follow special procedures for large-dollar deposits
- For deposits not subject to next-day availability, provide immediate availability of amounts up to \$100
- Make funds from certain checks, both local and nonlocal, available for withdrawal within the times prescribed by the regulation
- Provide exception notices about funds availability, including all required information.

The OTS in 1998 issued two formal enforcement actions that contained provisions relating to Regulation CC.

### Regulation DD (Truth in Savings)

The FFIEC agencies reported that 88 percent of institutions examined during the 1998 reporting period were in full compliance with Regulation DD. Institutions most frequently failed to comply with the following requirements:

- Provide appropriate maturity notices for certificates of deposit maturing in more than one year
- State required additional information in advertisements containing the annual percentage yield.

### Regulation AA (Unfair or Deceptive Acts or Practices)

The three bank regulators with responsibility for enforcing Regulation AA's Credit Practices Rule—the Federal Reserve, the OCC, and the FDIC—reported that 99 percent of the institutions examined during the 1998 reporting period were in compliance. The most frequent violation was failure to provide a clear, conspicuous disclosure regarding a cosigner's liability for a debt. No formal enforcement actions for violations of the regulation were issued during the period.

### Consumer Complaints

The Federal Reserve investigates complaints against state member banks and forwards to the appropriate enforcement agencies complaints that involve other creditors and businesses (see table). The Federal Reserve also monitors and analyzes complaints about unregulated practices.

### Complaints against State Member Banks

In 1998 the Federal Reserve received 3,889 complaints: 3,108 by mail, 760 by telephone, 14 electronically, and 7 in person. Fewer than half of the complaints (1,643) were against state member banks; of these, almost two-thirds involved unregulated practices. Of the complaints against state member banks, about 71 percent concerned lending; 3 percent alleged discrimination on a prohibited basis, and 68 percent addressed a variety of other practices, such as the denial of credit on a basis not prohibited by law (for example, credit history or length of residence)

or the release or use of credit information. Another 20 percent involved disputes about interest on deposits and general deposit account practices; the remaining 9 percent concerned disputes about electronic fund transfers, trust services, or other miscellaneous practices (see table).

In 1998 the Federal Reserve also received 2,114 inquiries about consumer credit and banking policies and practices. In responding to these inquiries, the Board and the Reserve Banks gave specific explanations of laws, regulations, and banking practices and provided relevant printed materials on consumer issues.

### Unregulated Practices

Under section 18(f) of the Federal Trade Commission Act, the Board in 1998 continued to monitor complaints about banking practices that are not subject to existing regulations and to focus on those complaints alleging practices that may be unfair or deceptive. Of the 2,381

complaints received about unregulated practices, the five most numerous categories related to credit cards: penalty charges on accounts (154); miscellaneous problems involving credit cards (148); customer service problems (138); interest rates and terms (125); and debt collection tactics (79). The specific complaints within these categories concerned such matters as creditors' failure to close accounts as requested; penalty charges, including over-limit fees; increased interest rates on accounts; and changed credit terms on pre-approved accounts. Each of these five complaint categories accounted for a small portion (4 percent or less) of all consumer complaints received by the Federal Reserve.

### Complaint Referrals to and by HUD

In 1998, in accordance with a memorandum of understanding between the agencies, the Board referred to HUD five complaints about state member banks that alleged violations of the Fair Hous-

Consumer Complaints against State Member Banks and Other Institutions Received by the Federal Reserve System in 1998

Subject	State member banks	Other institutions <sup>1</sup>	Total
Regulation B (Equal Credit Opportunity) .....	59	39	98
Regulation E (Electronic Fund Transfers) .....	20	53	73
Regulation M (Consumer Leasing) .....	7	19	26
Regulation Q (Payment of Interest) .....	1	1	2
Regulation Z (Truth in Lending) .....	270	393	663
Regulation BB (Community Reinvestment) .....	0	4	4
Regulation CC (Expedited Funds Availability) .....	23	51	74
Regulation DD (Truth in Savings) .....	40	55	95
Fair Credit Reporting Act .....	102	301	403
Fair Debt Collection Practices Act .....	9	24	33
Fair Housing Act .....	0	1	1
Flood insurance .....	1	5	6
Regulations G, T, U, and X .....	0	0	0
Real Estate Settlement Procedures Act .....	2	28	30
Unregulated practices .....	1,109	1,272	2,381
<b>Total</b> .....	<b>1,643</b>	<b>2,246</b>	<b>3,889</b>

1. Complaints against these institutions were referred to the appropriate enforcement agencies.

ing Act. Investigations of these complaints (and of three others pending at year-end 1997) revealed no evidence of unlawful discrimination.

Also in accordance with the memorandum of understanding, during 1998 HUD referred two complaints involving state member banks to the Federal Reserve. By year-end the Federal Reserve had completed its investigation of one of the two complaints; the investigation revealed no evidence of unlawful discrimination.

### Complaint Program Activities

During 1998 the Board's consumer complaints staff completed work on the Complaint Analysis Evaluation System and Reports (CAESAR) system, a personal computer-based system that will consolidate and replace mainframe-based analysis tools. The Board uses CAESAR, scheduled to be implemented

in January 1999, to monitor the status and resolution of consumer complaints and inquiries received by the Federal Reserve. Along with other management tools, CAESAR produces reports that allow staff to analyze, by type of allegation, the discrimination complaints received by the Federal Reserve; to automatically generate response letters to individual complaints; and to analyze data to determine patterns and trends.

During 1998 individual staff members from the Reserve Banks continued to work at the Board for several weeks at a time to gain familiarity with complaint operations in Washington. Fourteen participants from eleven Reserve Banks participated in the program.

### Consumer Policies

Through its consumer policies program, the Board explores ways to protect consumers in the area of retail financial

Consumer Complaints Received by the Federal Reserve System, by Type and Function, 1998

Complaint	Complaints against state member banks					
	Total		Not investigated		Investigated	
	Number	Percent	Unable to obtain sufficient information	Explanation of law provided to consumer	Bank legally correct	
					No reimbursement or other accommodation	Goodwill reimbursement or other accommodation
Loans						
Discrimination alleged						
Real estate loans .....	9	1	0	0	6	0
Credit cards .....	26	1	0	5	6	2
Other loans .....	24	1	1	0	12	0
Discrimination not alleged						
Real estate loans .....	92	6	2	14	35	9
Credit cards .....	880	54	7	135	217	319
Other loans .....	135	8	0	30	55	14
Deposits .....	326	20	5	36	128	55
Electronic fund transfers .....	20	1	2	1	8	1
Trust services .....	14	1	1	6	3	2
Other .....	117	7	13	21	44	18
<b>Total .....</b>	<b>1,643</b>	<b>100</b>	<b>31</b>	<b>248</b>	<b>514</b>	<b>420</b>



services other than by regulation, and conducts research that bears directly on policymaking. During 1998 much of this work related to leasing. The Board researched and analyzed consumers' understanding of lease terms and conditions, and helped disseminate consumer information on the consumer leasing disclosure requirements that took effect in January 1998. More than 650,000 copies of the Board's publication *Keys to Vehicle Leasing—A Consumer Guide* have been distributed through trade associations and conferences, auto shows, and the media; and the Board's web site on consumer leasing has had almost 175,000 visits.

During 1998 the Board also participated on an interagency team working to educate consumers about basic financial services. The team has developed a package of materials, entitled *Helping People in Your Community Understand Basic Financial Services*, that commu-

nity educators can use in promoting direct deposit among recipients of federal benefits. In connection with this effort, the Board used data from its Survey of Consumer Finances to develop a profile of households that do not have transaction accounts with depository institutions.

For its work during 1998 on reform of the Truth in Lending Act and the Real Estate Settlement Procedures Act, the Board studied the credit shopping behavior of consumers. Using data from the Board's 1995 Survey of Consumer Finances and from the Survey Research Center's monthly surveys of consumers, staff members analyzed consumers' mortgage-shopping behavior and their understanding of mortgage terms and conditions; results were shared with other agencies and the public through meetings, conferences, and journal articles. Staff members also gathered qualitative information from consumer focus

#### Consumer Complaints Received—Continued

Complaints against state member banks						Referred to other agencies	Total complaints
Investigated					Pending, December 31		
Customer error	Bank error	Factual or contractual dispute—resolvable only by courts	Possible bank violation—bank took corrective action	Matter in litigation			
0	0	1	0	0	2	14	23
0	2	1	0	0	10	11	37
0	0	1	1	0	9	14	38
0	16	3	0	3	10	303	395
11	123	11	3	2	52	747	1,627
0	20	1	1	3	11	361	496
2	55	9	2	11	23	462	788
1	6	1	0	0	0	53	73
0	1	0	0	0	1	6	20
0	11	2	0	2	6	275	392
14	234	30	7	21	124	2,246	3,889

groups in Baltimore and northern Virginia; alternative disclosure formats for the annual percentage rate and contract interest rates, the good faith estimate given under the Real Estate Settlement Procedures Act, and the disclosures of guaranteed settlement costs were tested.

### **Consumer Advisory Council**

The Consumer Advisory Council convened in March, June, and October to advise the Board on matters concerning laws that the Board administers and other issues related to consumer financial services. The council's thirty members come from consumer and community organizations, the financial services industry, academic institutions, and state government agencies. Council meetings are open to the public.

The implementation of the Community Reinvestment Act was addressed at each of the three meetings. In March the council focused on perceived problems with uniformity among the supervisory agencies in evaluating the CRA performance of their respective institutions under the revised CRA regulations. In recognition of these issues, the agencies were taking steps to help assess the uniformity of their approaches. At all three meetings the council discussed the challenges faced by institutions and examiners in delineating an institution's CRA assessment area. This issue is significant for numerous banks, such as national institutions that have only one branch or main office, consumer lenders that have loan production offices but no deposit-gathering branches, and Internet banks that have no branch or main office. Council members voiced concerns that de-emphasizing geography might adversely affect low- and moderate-income persons and those in rural areas who do not have access to electronic distribution systems. Other CRA issues

discussed by the council included how the lending test accounts for loans originated and purchased, bank performance under the investment and service tests, and use of the strategic plan option by financial institutions.

In March the council discussed legislative recommendations being developed to simplify, consolidate, and streamline regulations implementing the Truth in Lending Act and the Real Estate Settlement Procedures Act. (See "TILA and RESPA Reform.") The discussion focused on the timing and feasibility of providing firm mortgage loan cost estimates that would enable consumers to make meaningful cost comparisons when they shopped for loans. The accuracy of early disclosures was a particular concern. Some members believe that the existing good faith estimate, provided within three days of a mortgage loan application, gives reasonable certainty about closing costs. Others expressed interest in reform proposals in which the lender might guarantee both the interest rate and closing costs. In June the council reviewed remedies that protect consumers when the timing or content of the disclosures is improper or defective. Concerns that twenty-four states do not require the sending of a notice of foreclosure to a debtor who is in default, and that only nineteen states give the homeowner a statutory right to cure a default, led the council to consider whether there should be a federally required notice and a right-to-cure.

Also in June the council discussed the collection of data on the race and sex of applicants for consumer loans other than mortgages. Regulation B currently prohibits such collection. The council focused on whether lenders should be required, or allowed, to collect such data. Some members favored, and others opposed, mandatory data col-

lection. Some preferred letting lenders collect the data voluntarily. It was suggested that either mandatory or voluntary collection could provide useful data in marketing and fair lending, could help lenders create targeted marketing programs, and could facilitate referrals for special credit programs. Council members' concerns about the data collection included cost burdens, problems in identifying an applicant's characteristics when the applicant does not volunteer the information, and difficulties in characterizing the characteristics when a firm applying for a small-business loan has multiple owners. The council also discussed the benefits and disadvantages of requiring that pre-approvals or pre-qualifications for home mortgage loans be reported in the HMDA data. Currently, a preliminary evaluation of a potential applicant's creditworthiness is not reported.

The council also addressed issues concerning the substitution of electronic delivery of consumer disclosures for traditional paper copies. The Board's interim rule governing electronic fund transfer, issued in March 1998, permits depository institutions to deliver certain disclosures electronically if the consumer agrees. (See "Regulatory Matters.") Council members provided a variety of comments on electronic delivery of federal disclosures. For example, some believed that consumers should have a right to paper copies of certain disclosures upon request. Some were concerned about creditors providing certain notices electronically, such as the TILA right of rescission. Others were concerned about ensuring that consumers make informed decisions about receiving disclosures electronically.

At its October meeting the council considered how the use of credit scoring systems was affecting consumer and small business lending. Members noted

that credit scoring provides many benefits, including significant efficiencies that reduce lender costs while helping to minimize subjectivity in loan decisions; but credit scoring has also raised a number of issues. Council members noted that credit scoring can have fair lending implications. For example, some members suggested that unequal access to credit by minorities could bias or distort the data used in a scoring model.

In October, the council also discussed barriers to lending and reinvestment efforts by financial institutions on Indian reservations. Council members noted that Indian Country is perceived to be among the most underserved credit and banking service markets in the nation. One critical restraint to economic and community development on Indian reservations is that each tribe is a sovereign nation with its own commercial laws that affect creditors' rights.

### **Testimony and Legislative Recommendations**

In June the Board testified before the House Committee on Commerce on developments in electronic commerce generally, and electronic payments specifically. The testimony noted that new payment products, such as stored-value cards and electronic cash for use on the Internet, are designed to substitute for existing payment methods such as cash, checks, and credit and debit cards; thus, to gain acceptance, they will likely need to offer consumers and businesses significantly improved features in terms of cost and convenience. Although anticipating that the effect of the emerging electronic payment methods on the Board's core responsibilities will be minimal in the near term, the Board cautioned that technological change and the growth of electronic commerce

could raise complex policy issues that may require careful monitoring.

In July the Board testified before the House and Senate Banking Committees on ways to improve the disclosures required for home mortgage loans under the TILA and to unify them with the disclosures required under RESPA. The Board's testimony discussed the joint report issued by the Board and the Department of Housing and Urban Development, which provided a framework for simplifying and streamlining the information given to consumers in the mortgage lending process. (See "TILA and RESPA Reform.")

### **Recommendations of Other Agencies**

Each year the Board asks for recommendations from the other federal supervisory agencies for amending the consumer financial services laws or the implementing regulations.

The OCC believes that despite legislative and regulatory efforts to reduce compliance burden, the rules and disclosure requirements under the consumer financial services laws remain complex for consumers and costly for creditors. Accordingly, the OCC suggests that the Congress consider alternatives to provide more meaningful disclosures to consumers that are less burdensome to depository institutions. In addition, the OCC recommends that the Congress consider modifications to

the referral requirements in the ECOA. The OCC suggests, for example, limiting mandatory referrals to specific prohibited bases, authorizing the Department of Justice to relieve an agency from mandatory referral requirements, or authorizing agency waiver of referral if detected violations stem from self-assessments.

The FTC supports the Board's current review of Regulation B and would support any similar effort to update and clarify Regulation Z. The FDIC supports amending Regulations B, M, Z, and DD to allow for the electronic delivery of certain disclosures. The FDIC also expresses concern about the predatory marketing practices of some subprime credit-card lenders, and in this regard supports the development of regulatory or legislative changes to Regulation Z or Regulation AA that would enable the agencies to supervise current trade practices more effectively.

### **Year 2000 Initiatives**

During 1998 the Board made a major effort to ensure that the hardware and software systems it uses in connection with consumer and community affairs matters are Year 2000 compliant. Among other things, it revised certain systems and converted them from a mainframe environment to a personal-computer environment. Certification of compliance is scheduled for March 1999. ■